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CHINA: QUARTERLY ECONOMIC REPORT

First Quarter: Investment, Heavy Industry Surge;
Winter Wheat Prospects Good

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Summary

During the first quarter, large unplanned investment continued to divert construction materials from key energy and transportation projects; the associated surge in heavy industry continued to squeeze consumer goods production. Favorable weather and an increase in sown area almost guarantee another record harvest of winter wheat. Returns from the spring Guangzhou trade fair indicate, as we have been expecting, large gains in Chinese imports accompanied by negligible growth in exports during coming months.

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Industry

Industrial production, primarily producer goods output, rose at a 6.9 percent rate in first quarter 1983. This was well above the planned rate of 4 percent and contributed to a number of unwelcome developments. In late March, Beijing stepped up its criticism of industrial performance, citing the squeeze on consumer goods production and poor "economic results."

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Heavy industry grew by 11.7 percent in Jan-Mar, triple the 3.9 percent annual target. Machinery output was up sharply;

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This memorandum was prepared by [redacted] the Domestic Policy Branch of the China Division of the Office of East Asian Analysis, Deputy Directorate of Intelligence. Questions and comments are welcome and may be directed to the authors [redacted]

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production by factories under the Ministry of Machine Building rose by 21 percent. (We estimate that more than half of 1982's 9.9-percent increase in heavy industry came from the machine building industries.) Steel output was up by nearly 10 percent, despite efforts to hold production at last year's levels. Activity in both sectors reflected strong--from Beijing's standpoint, undesirably strong--investment demand. Energy production rose by 4.8 percent, largely on the strength of a 5.6-percent gain in coal production. Crude oil output also rose (2.1 percent). [REDACTED] 25X1

Light industry in contrast grew by a weak 2.5 percent in the first quarter. The goal for the year is 4.1 percent. Part of the problem, according to Beijing, was that some energy, raw materials, and transportation that should have been used in light industry instead went to heavy industry. Consumer goods industries are also suffering from an inability to produce the type and quality of goods that today's more selective Chinese consumers want. [REDACTED] 25X1

Despite the priority ostensibly given "economic results"--quality improvements and the reduction of energy and raw materials consumption--industry's record in these areas remains poor. Beijing collects data on 75 indices measuring various quality aspects of industrial products. In the first quarter, only 23 of these indices--31 percent--showed some improvement. Similarly, of 105 indices of energy and materials consumption, only 36--34 percent--showed signs of progress. Aside from the implications for consumer satisfaction and wasteful use of resources, continuing problems in these areas have contributed, via a fall-off in industrial profits (down almost 6 percent) to a reduction in state revenues. [REDACTED] 25X1

Agriculture

An unusual pattern of cool, wet weather and hailstorms delayed both the planting and harvesting of the early rice crop in South China. Hunan Province was hardest-hit: crops were destroyed on over 500,000 hectares, roughly 10 percent of the province's sown area. We expect a sizeable decline in the nation's early rice harvest, the first of three annual rice crops. [REDACTED] 25X1

Foreign Trade

The Guangzhou fair traditionally serves as a forum for promoting Chinese exports. But this year Chinese import orders at the spring fair were 24 percent higher than orders last fall, while exports rose by only 1 percent. Agreements signed reportedly exceeded \$2 billion. Chemicals, mostly agricultural, from the United States and Japan accounted for most of the growth in import orders. Buyers from the provinces also sought instruments, machinery, and equipment, particularly from US

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manufacturers, who offered lower prices and higher quality than the Japanese. Hong Kong and Macau purchases accounted for 45 percent of China's export sales. [] 25X1

Elsewhere in the Economy

Investment: Despite plans for a 9-percent reduction in 1983, capital construction (new fixed investment) was up 21 percent over first-quarter 1982 and continued to exert a strong pull on producer goods industries. One favorable development is evident: spending was particularly heavy on projects related to energy (up 29 percent) and transportation (up 89 percent), together constituting 40 percent of first-quarter investment. Other investment, much of it in low priority facilities, showed a sizable, 8 percent increase, which hampered the completion of high priority projects. [] 25X1

Transportation: Performance was good, with rail freight up 5.6 percent. The amount of coal hauled exceeded the plan target, easing energy supply problems. While water cargo transport was up only 2.5 percent, freight handling at major coastal ports rose by 5.5 percent. (U) [] 25X1

Retail Sales: Sales of consumer goods soared 12 percent, boosted by large increases in rural incomes following last year's extraordinarily strong agricultural performance and by urban wage increases legislated last October. [] 25X1

Housing: Starts in urban areas began to drop off, compared with first-quarter 1982; but--a good sign--completions rose 15 percent. [] 25X1

Budget: Rising industrial costs (up 2.6 percent) and lower profits (down 5.8 percent) hurt first-quarter revenues, which apparently fell below Beijing's projections. A pessimistic outlook for revenues may help explain the apparent urgency in the shift to a revenue system based largely on taxes--effective 1 June. [] 25X1

Performance Outlook

Beijing's statements about the economic situation have become increasingly critical. Press editorials have mentioned the possibility of another readjustment if the diversion of construction materials and production inputs away from priority projects and light industry continues. The inability to curb spending by localities and enterprises last year and the subsequent failure to meet 1982 investment targets for energy and transportation appear to have convinced Beijing that the situation calls for bolder actions. This is certainly the impression one gets from speeches and comments at the just-concluded session of the National People's Congress. [] 25X1

But as we have seen before, criticism by the central

leadership does not automatically translate into corrective action. Following an industrial conference in late March, there have been signs of improvement in light industry: in April and May, output grew by 7.3 percent and 8.2 percent, respectively, compared with 2.5 percent for Jan-Mar. But this acceleration is too brief to regard as a full-fledged turnaround in the light industrial sector. In coming months we expect largely a continuation of recent trends:

- higher-than-planned investment, with critical projects still unable to get adequate supplies of building materials;
- heavy industrial growth exceeding the plan target;
- further problems with light industry, attributable to shortages of inputs and the inability of manufacturers to produce the type of products that consumers now want;
- a tendency of factory managers to ignore quality and costs--which reduces sales and profits, and in turn diminishes budget revenues. 25X1

Agriculture. Prospects for the winter grain harvest (mostly wheat) are excellent again this year, following last year's record 68.4-million-ton wheat harvest. Winter wheat regions have had excellent weather since plantings began last fall, and initial reports indicate an expansion in sown area of at least 1.2 million hectares, roughly 5 percent. 25X1

Foreign trade. Exports will probably again show a seasonal downturn during the first half of 1983, perhaps ameliorated somewhat by a recovery in the West. Imports are scheduled to rise 40 percent during the year, but so far they have remained at 1982 levels. Nevertheless, on the basis of deals concluded at the spring and fall Guangzhou trade fairs, which serve as indicators of trade for the year, we expect a large increase in imports during 1983. The small gain in export orders reinforces Beijing's own estimate that this year's exports will remain largely unchanged from last year. 25X1

	Quarters					Annual		
	1982				1983	1982		1983
	I	II	III	IV	I	Chinese Plan	Actual	Chinese Plan
Production (Bil 1980 Yuan, except where noted; numbers in parentheses are percent change from previous year)								
Total Industry	129.16 (11.5)	143.77 (8.9)	136.24 (5.7)	148.71 (4.1)	138.29 (7.1)*	538.9 (4.0)	557.9 (7.7)	580.2 (4.0)
Heavy Industry	62.07 (8.5)	72.09 (10.4)	69.51 (10.4)	72.73 (7.9)	69.33 (11.7)	254.0 (1.0)	276.4 (9.9)	287.2 (3.9)
Light Industry	67.25 (14.6)	71.52 (7.3)	66.73 (0.0)	75.98 (1.6)	68.96 (2.5)	284.9 (7.0)	281.5 (5.7)	293.0 (4.1)
Agricultural Production						240.4 (4.0)	256.6 (11.0)	266.9 (4.0)
Grain Production (Million tons)						333.5 (2.6)	353.4 (8.7)	N.A.
Energy Production								
(Million tons coal equivalent)	154.16 (10.0)	168.1 (8.0)	164.6 (5.6)	181.14 (-5.2)	162.19 (5.2)	625.4 (-0.3)	668.0 (5.7)	N.A.
Oil Production (Million tons)	25.34 (1.4)	26.06 (3.5)	25.44 (0.6)	25.28 (-0.9)	25.88 (2.1)	100.0 (-1.2)	102.12 (0.9)	100.0
Seasonally Adjusted Production Data (Numbers in parentheses are percent change over previous quarter, at annual rate)								
Industrial Production	137.42 (6.5)	138.25 (2.4)	139.31 (3.1)	142.72 (10.1)	147.07 (12.8)			
Heavy Industry	66.69 (9.6)	68.17 (9.2)	69.57 (8.5)	71.82 (13.6)	74.48 (15.6)			
Light Industry	70.75 (4.9)	69.96 (-4.4)	69.23 (-4.1)	71.47 (13.6)	72.52 (6.0)			
Energy Production								
(Million tons coal equivalent)	164.39 (5.2)	166.33 (4.8)	167.36 (2.5)	169.61 (5.5)	173.00 (8.2)			
Oil Production (Million tons)	25.68 (6.7)	26.01 (5.2)	25.29 (-10.7)	25.15 (-2.2)	26.23 (18.3)			

*Quarterly growth rates shown in the table may differ from the official growth rates cited in the text. The difference is caused by unannounced revisions of data for earlier quarters by the Chinese State Statistical Bureau.

(Percent change from previous year in parentheses)

	Quarters					Annual		
	1981	1982				1980	1981	1982
	IV	I	II	III	IV			
<u>U.S. - China Trade</u>	(Mil \$US, f.o.b., not seasonally adjusted, except where noted)							
Exports to U.S.	485.8 (55.5)	556.6 (47.0)	487.6 (-0.5)	697.0 (29.6)	542.4 (11.7)	1053.3 (78.2)	1892.0 (79.6)	2283.6 (20.7)
Textiles and Clothing	169.6 (65.5)	200.6 (39.6)	175.4 (44.0)	261.4 (44.8)	188.5 (11.1)	354.6 (78.5)	615.6 (73.6)	825.9 (34.2)
Petroleum and Products	93.7 (160.3)	114.3 (412.6)	95.6 (69.2)	214.7 (77.6)	173.1 (84.7)	134.7 (39.6)	293.5 (117.9)	597.7 (103.7)
Imports from U.S.	922.3 (-21.8)	905.2 (-23.5)	801.9 (18.1)	686.6 (-16.1)	518.6 (-43.8)	3754.4 (117.8)	3602.8 (-4.0)	2912.3 (-19.2)
Grain (million tons)	2.355 (-20.3)	1.968 (0.3)	2.564 (90.9)	2.407 (-0.7)	1.527 (-35.2)	8.037 (101.2)	8.084 (0.6)	8.466 (4.7)
Textile Fibers	253.3 (-1.8)	237.1 (-46.9)	94.2 (-46.3)	37.6 (-79.0)	26.5 (-89.5)	1016.4 (127.0)	1053.5 (3.7)	395.3 (-62.5)
Trade Balance with U.S.	-436.5	-348.6	-314.3	10.4	23.8	-2701.1	-1710.8	-628.7
<u>Aggregate Indicators</u>								
Population (mil on July 1)						981 (1.3)	993 (1.2)	1008 (1.5)
Gross National Produce (Bil 1982 \$US)						271.8 (5.2)	280.0 (3.0)	300.7 (7.4)
GNP per capita (1982 \$US)						277.1 (5.5)	282.0 (1.8)	298.3 (5.8)
State Budget (Bil1 yuan):								
Revenues						108.5 (-1.6)	109.0 (0.5)	110.7 (1.6)
Expenditures						121.3 (-10.6)	111.5 (-8.1)	113.7 (2.0)
Deficit (-) or Surplus (+)						-12.8	-2.5	-3.0

(Percent change from previous year in parentheses)

	Quarters					Annual		
	1981	1982				1980	1981	1982
	IV	I	II	III	IV			
<u>International Trade and Finance</u>	<u>(Mil \$US, f.o.b., not seasonally adjusted, except where noted)</u>							
Total Exports	6020.1 (8.7)	5569.9 (14.4)	5538.2 (5.2)	5673.6 (3.4)	5577.8 (-7.4)	18924.7 (40.4)	21642.7 (14.4)	22359.2 (3.3)
Total Imports	4250.1 (-29.8)	4073.8 (-25.8)	4108.5 (-4.2)	3872.5 (-1.2)	4026.3 (-5.3)	19303.9 (34.1)	17944.5 (-7.0)	16081.2 (-10.4)
Trade Balance	1770.0	1496.1	1429.7	1801.1	1551.5	-379.2	3698.4	6278.0
Oil and Petroleum Products Exports	1289.6 (0.3)	1196.9 (14.4)	1047.2 (-4.5)	1303.5 (12.1)	1272.6 (-1.3)	4165.1 (84.5)	4595.4 (10.3)	4820.4 (4.9)
Grain Imports (Million tons)	3.357 (-12.5)	3.209 (-4.7)	4.165 (30.7)	3.954 (20.2)	3.656 (8.9)	13.673 (26.0)	13.204 (-3.4)	14.984 (13.5)
Liquid Assets*	5048 (98.3)	5460 (129.8)	7287 (90.7)	9444 (139.9)	11339 (124.6)	2545	5048	11339
Liquid Liabilities*	4759 (-16.0)	3719 (-41.3)	3697 (-38.3)	3724 (-37.4)	3745 (-21.3)	5667	4759	3745
Exchange Rate (yuan/ dollar)	1.7455	1.8675	1.9310	1.9684	1.9227	1.5115	1.7183	1.9224
<u>Japan - China Trade</u>								
Exports to Japan	1491.6 (25.3)	1299.9 (24.8)	1250.3 (4.0)	1250.6 (-3.5)	1282.6 (-14.0)	4139.5 (48.3)	5031.9 (21.6)	5083.4 (1.0)
Petroleum and Products	770.6 (20.9)	716.1 (30.0)	572.0 (-1.9)	704.0 (0.1)	711.8 (-7.6)	2159.4 (104.6)	2607.7 (20.8)	2703.0 (3.7)
Imports from Japan	1147.4 (-37.5)	848.6 (-40.7)	888.2 (-34.0)	839.6 (-27.1)	923.5 (-19.5)	5109.6 (38.8)	5076.1 (-0.7)	3500.0 (-31.1)
Trade Balance with Japan	344.1	451.3	362.1	410.9	359.1	-969.9	-44.2	1583.4

*Liquid assets are almost all foreign exchange reserves; liquid liabilities are mainly national bank liabilities. In addition, the Chinese have some SDRs and IMF liabilities and 12.7 million ounces of gold.

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